UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Curt Hébert, Jr., Chairman;
William L. Massey, Linda Breathitt,
and Pat Wood III.

Public Utilities Commission of the State of California	Docket Nos. RP00-241-000 and RP00-241-004

v.

El Paso Natural Gas Company,
El Paso Merchant Energy-Gas, L.P.,
and El Paso Merchant Energy Company

ORDER ON REHEARING

(Issued June 11, 2001)

On April 4, 2000, the Public Utilities Commission of the State of California (CPUC) filed a complaint under section 5 of the Natural Gas Act (NGA)[1] against El Paso Natural Gas Company (El Paso Pipeline), as well as El Paso Merchant Energy-Gas, L.P. and El Paso Merchant Energy Company (jointly, El Paso Merchant). CPUC asserted, inter alia, that three transportation contracts between El Paso Pipeline and El Paso Merchant for approximately 1,220 MMcf/day of firm transportation capacity to California (El Paso Contracts) raised issues of possible affiliate abuse, of anticompetitive impact on the delivered price of gas and the wholesale electric market in California, and of the effectiveness of the Block II recall rights established in El Paso Pipeline's 1996 settlement with its transportation customers (El Paso Settlement). CPUC subsequently filed a motion for summary disposition.

On March 28, 2001, the Commission issued an Order Denying Motion for Summary Disposition, Dismissing Complaint in Part, and Setting It for Hearing in Part

[1] 15 U.S.C. § 717d (1994).

(March 28, 2001 order).[2] In that order the Commission found, inter alia, that El Paso Pipeline and El Paso Merchant did not violate the Commission's Standards of Conduct for Interstate Pipelines with Marketing Affiliates (Affiliate Standards)[3] in negotiating and entering into the El Paso Contracts. The Commission also concluded that El Paso Pipeline's open season process was not skewed to favor a bid by El Paso Merchant and that El Paso Merchant did not possess information regarding a discount that was unavailable to other bidders. However, the Commission set for hearing on an expedited basis the question of whether El Paso Pipeline and/or El Paso Merchant had market power, and if so, exercised it to drive up the price of natural gas at the California border.

A. Requests for Rehearing

CPUC, El Paso Pipeline, El Paso Merchant, and Pacific Gas and Electric Company (PG&E) jointly with Southern California Edison Company (Edison) filed timely requests for rehearing of the March 28, 2001 order.

CPUC contends that the Commission erred in (1) failing to require that the El Paso Contracts be filed for Commission approval under NGA section 4, (2) finding that El Paso Merchant did not receive secret and material information from its affiliate Mojave Pipeline Company (Mojave) during the open season, and (3) finding that El Paso Pipeline's open season was not skewed to favor El Paso Merchant.

PG&E and Edison also argue that the El Paso Contracts should have been filed for Commission approval under NGA section 4. In addition, they maintain that the Commission erred in dismissing the allegations of affiliate abuse without a hearing and that the Commission should have required El Paso Pipeline and El Paso Merchant to comply with the terms of the El Paso Settlement with respect to recall rights under the Block II contract.

On rehearing, El Paso Pipeline and El Paso Merchant assert that the Commission erred in setting the market power issue for hearing. Both El Paso Pipeline and El Paso Merchant contend that the Commission should have dismissed CPUC's complaint in its entirety because CPUC and the intervenors failed to meet the burden of proof imposed by NGA section 5.

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[2] Public Utilities Commission of the State of California v. El Paso Natural Gas Co., 94 FERC ¶ 61,338 (2001).

[3] 18 C.F.R. Part 161 (2000).

B. Report to Commission, Request to Waive Initial Decision Date, and Request for Guidance

In a report issued May 31, 2001, the Chief Administrative Law Judge (Chief Judge), citing the complexity of this proceeding, the extensive hearing record already compiled, and a unanimous request by the parties, asked the Commission to waive the date established for an initial decision in this proceeding. On June 4, 2001, the Commission granted the request of the Chief Judge and extended the deadline for the initial decision until September 4, 2001.

In his May 31, 2001 report, the Chief Judge also sought guidance from the Commission with respect to the scope of the hearing on the market power issue. The Chief Judge asked the Commission to clarify whether its finding in the March 28, 2001 order of no violation of the Commission's Affiliate Standards was based solely on the record before the Commission at the time of the March 28, 2001 order and whether the Commission intended that he compile a more complete record on the question of possible violations of the Affiliate Standards and make findings as to whether any such violation, if it existed, contributed to the alleged exercise of market power by El Paso Pipeline and El Paso Merchant.

On June 5, 2001, El Paso Pipeline filed comments on the May 31, 2001 report by the Chief Judge. El Paso Pipeline asserts that (1) the Commission already has reviewed thoroughly the issues relating to the Affiliate Standards; (2) no evidence has emerged at the hearing that is inconsistent with the Commission's findings concerning affiliate issues in the March 28, 2001 order; (3) the affiliate rulings are subject to rehearing at the Commission level and need not be interjected into the hearing; and (4) if the scope of the hearing is expanded to include compliance with the Affiliate Standards, the parties must be afforded the opportunity to file new testimony regarding all allegations of affiliate abuse.

As discussed below, the Commission grants in part and denies in part the requests for rehearing of the March 28, 2001 order filed by CPUC, PG&E, and Edison and sets for hearing the allegations of affiliate abuse and violations of the Affiliate Standards raised by complainants. The Commission denies the requests for rehearing of the March 28, 2001 order filed by El Paso Pipeline and El Paso Merchant.

Background

The March 28, 2001 order contains a detailed description of the background of this proceeding, which is summarized briefly here to the extent necessary for purposes of this order. The capacity at issue in this case was turned back permanently to El Paso Pipeline by California local distribution companies (LDCs) in the early 1990s when there was a considerable amount of excess pipeline capacity into California. In order to resolve El Paso Pipeline's efforts to mitigate the loss of revenue resulting from the capacity turnback, various parties, including CPUC, entered into the El Paso Settlement. In part, that settlement established the three blocks of capacity that are covered by the El Paso Contracts. The March 28, 2001 order also describes the El Paso Settlement and previous Commission proceedings relating to contracts covering the three blocks of capacity between El Paso Pipeline and the predecessor of Dynegy Marketing and Trade (Dynegy) and between El Paso Pipeline and Enron North America Corp. (Enron).

In its complaint, CPUC asked the Commission to terminate the El Paso Contracts or to require El Paso Merchant to release on a short-term basis any unused firm transportation rights under those contracts to replacement shippers offering a higher rate than El Paso Merchant is obligated to pay El Paso Pipeline. CPUC further requested that the Commission order El Paso Pipeline to remove certain restrictions in the Block II contract. In its August 31, 2000 motion for summary disposition, CPUC also urged the Commission to abrogate the El Paso Contracts, to prohibit El Paso Pipeline from tying together Block I, Block II, and Block III capacity in a "total package" arrangement in subsequent open seasons or prearranged agreements, and to prohibit El Paso Merchant or any other El Paso Pipeline affiliate from bidding on or subscribing to the Block I, Block II, or Block III capacity.

Discussion

As discussed below, the Commission grants in part and denies in part the requests for rehearing filed by CPUC, PG&E, and Edison. The Commission finds that El Paso Pipeline was not required to file the El Paso Contracts for Commission approval under NGA section 4. However, in addition to the issues previously set for hearing, the Commission now sets for hearing the issue of whether El Paso Pipeline and/or El Paso Merchant engaged in affiliate abuse or violated the Affiliate Standards in bidding for or awarding the El Paso Contracts, including the transportation discount granted by Mojave. The Commission denies the requests for rehearing of El Paso Pipeline and El Paso Merchant, which argued that the Commission should have dismissed CPUC's complaint in its entirety.

A. Additional Matters Set for Hearing

As stated above, in his May 31, 2001 report, the Chief Judge sought guidance from the Commission with respect to the scope of the hearing on the market power issue. The Chief Judge asked the Commission to clarify whether the Commission's finding of no violation of the Affiliate Standards was based solely on the record before the Commission at the time of the March 28, 2001 order and whether the Commission intended that he compile a more complete record on the question of possible violations of the Affiliate Standards and make findings as to whether any such violation, if it existed, contributed to the alleged exercise of market power by El Paso Pipeline and El Paso Merchant. As also stated above, El Paso Pipeline filed comments contending that no additional evidence is necessary on the issue of affiliate abuse and the alleged violations of the Affiliate Standards.[4]

In their requests for rehearing, CPUC, PG&E, and Edison claim that El Paso Merchant had secret and material information that was unavailable to other potential bidders, thereby tainting the process. CPUC asserts that it is undisputed that, during the

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[4]Standard of Conduct F requires that a pipeline that provides to its marketing affiliate information relating to natural gas transportation must provide that information contemporaneously to all potential shippers, affiliated and nonaffiliated, on its system. 18 C.F.R. § 161.3(f) (2000). In Order No. 497-A, the Commission stated that, "[i]f a pipeline and its affiliate's operating personnel are functioning independently, a pipeline's communications with the affiliate should be limited to specific information regarding the affiliate's transportation request or service...." In an example illustrating its position, the Commission stated, "Apart from the general reporting requirement of section 250.16 or other applicable rules, [the] pipeline ... would not have to disclose the information transmitted to the marketing affiliate to perfect the transportation request or complete the transportation transaction." Inquiry into Alleged Anticompetitive Practices Related to Marketing Affiliates of Interstate Pipelines; Order on Rehearing, Order No. 497-A, FERC Stats. & Regs., Regulations Preambles 1986-1990 ¶ 30,868 at 31,596-97 (1989).

Standard of Conduct G provides that, to the maximum extent practicable, the pipeline must require its operating employees and those of its marketing affiliate to function independently of each other. 18 C.F.R. § 161.3(g) (2000). In its interpretation of the term "operating employee," the Commission emphasized that, "[u]nder normal circumstances, employees, including highly-placed operatives such as members of the board of directors or officers of the corporations, who do not have [day-to-day operating] duties would not be likely to receive or use transportation-related information subject to Standard F." Inquiry into Alleged Anticompetitive Practices Related to Marketing Affiliates of Interstate Pipelines and Ozark Gas Transmission System; Order on Rehearing and Extending Sunset Date, Order No. 497-E, FERC Stats. & Regs., Regulations Preambles January 1991 - June 1996 ¶ 30,987 at 30,996 (1993). Accord Amoco Production Company v. Natural Gas Pipeline Company of America, 83 FERC ¶ 61,197 (1998).

open season, El Paso Merchant negotiated lower rates for large volumes utilizing Mojave's IT rates to Wheeler Ridge, and that no other party knew of this discount until after the close of the open season.[5] They further contend that the open season was skewed to favor a bid by El Paso Merchant in a variety of ways. CPUC, PG&E, and Edison generally argue that the Commission misinterpreted the evidence relating to the open season and the discount on which it relied in the March 28, 2001 order and failed to provide an adequate explanation of the basis for its decision not to address the issue of affiliate abuse at a hearing.

In consideration of the Chief Judge's request for guidance with respect to the affiliate issues and the requests for rehearing filed by CPUC, PG&E, and Edison, the Commission has determined to set for hearing the issues raised by CPUC's complaint concerning allegations of affiliate abuse and violation of the Affiliate Standards. The Commission now believes these allegations raise factual issues that are best resolved in an evidentiary hearing.

B. Whether the El Paso Contracts Should Have Been Filed for Commission Approval

CPUC, PG&E, and Edison contend that the El Paso Contracts should have been filed for Commission approval under NGA section 4. CPUC argues that this is particularly true when the contracts cover such a large amount of capacity, are between affiliates, and have potentially anticompetitive implications.

CPUC, PG&E, and Edison state that the El Paso Contracts do not follow the pro forma service agreements in El Paso Pipeline's tariffs. Specifically, they contend that section 9.5 of the Block I contract constitutes a material deviation from the pro forma service agreement: it allows El Paso Merchant the option of switching to maximum rates in order to obtain primary receipt points in the Permian and Anadarko Basins. CPUC,

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[5]CPUC cites Ex. PUC-19 and Mojave's response to the Commission Staff's Data Request No. 4 (filed as an attachment to Motion for Leave to File Answer and Answer of the Public Utilities Commission of the State of California to Respondents' Answers to the Motion for Summary Disposition, October 16, 2000). CPUC contends that the Mojave discount was important for the use of Block II El Paso Pipeline capacity. CPUC cites the Answer of El Paso Merchant Energy Company to the Complaint of Public Utilities Commission of the State of California, May 1, 2000, at 32, where El Paso Merchant states that it "would very much appreciate a discount on Mojave so that it can flow to the SoCalGas market through Wheeler Ridge in order to deal with the primary delivery point restrictions placed on the Block II capacity by the FERC."

PG&E, and Edison point out that El Paso Merchant obtained all of the Block I capacity at $.04 per MMBtu, far less than El Paso Pipeline's maximum tariff rate, but that the Block I contract contained this unique option, which El Paso Merchant exercised as of November 21, 2000. According to PG&E and Edison, under Commission Order No. 582,[6] this material deviation triggered an obligation for El Paso Pipeline to file for Commission scrutiny all three of the contracts, which El Paso Pipeline itself characterized as a package deal.

CPUC, PG&E, and Edison state that section 4.5(b)(i) of the General Terms and Conditions (GT&C) of El Paso Pipeline's tariff provides that a bidder obtains primary receipt points from the Permian and Anadarko Basins only if it agrees to pay the maximum tariff rates. In addition, continue CPUC, PG&E, and Edison, the pipeline's February 2000 open season rules relating to bids for the Block I capacity provided that, in the event the Block I capacity was awarded at a rate less than the applicable maximum tariff rate, the capacity would have only alternate receipt point rights from all receipt points.[7]

CPUC, PG&E, and Edison challenge El Paso Pipeline's reliance on section 154.1(d) of the Commission's regulations as the basis for its claim that the contracts do not contain a material deviation from the pro forma service agreement that would require Commission approval under section 4. CPUC, PG&E, and Edison contend that the history of section 154.1(d),[8] shows that it cannot be used to waive the section 4 filing requirement in this case. PG&E and Edison further argue that a section 4 analysis of the El Paso Contracts is required by Opinion No. 256, which they cite for the principle that the Commission cannot automatically apply a waiver-type regulation in a manner that prevents the Commission from conducting a meaningful review of a transaction.[9]

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[6] Filing and Reporting Requirements for Interstate Natural Gas Company Rate Schedules and Tariffs, Order No. 582, FERC Stats. & Regs., Regulations Preambles January 1991 - June 1996 ¶ 31,025 (1995), order on reh'g, Order No. 582-A, FERC Stats. & Regs., Regulations Preambles January 1991 - June 1996 ¶ 31,034 (1996).

[7] CPUC cites Ex. PUC-12 at 3.

[8] 18 C.F.R. § 154.1(d) (2000).

[9] PG&E and Edison cite Natural Gas Pipeline Company of America, Opinion No. 256, 37 FERC ¶ 61,215 (1986), order on reh'g, Opinion No. 256-A, 39 FERC ¶ 61,218 at 61,767 (1987), order on reh'g, Opinion No. 256-B, 39 FERC ¶ 61,218 (1987), aff'd sub nom., TransCanada PipeLines Ltd. v. FERC, 878 F.2d 401 (D.C. Cir. 1989).

Moreover, argue CPUC, PG&E, and Edison, when this capacity previously was acquired by third parties, the Commission scrutinized the applicable transportation agreements pursuant to NGA section 4. Indeed, claim CPUC, PG&E, and Edison, in its orders addressing the Dynegy and Enron contracts, the Commission recognized that there may be potentially anticompetitive effects from the sale of such a large block of capacity to a single party, and the Commission confirmed that these competitive concerns would be examined in subsequent proceedings.[10]

The Commission finds no merit to the arguments that the El Paso Contracts should have been filed for Commission approval pursuant to NGA section 4. Section 154.1(d) of the Commission's regulations provides in pertinent part that "[a]ny contract or executed service agreement which deviates in any material aspect from the form of service agreement in the tariff is subject to the filing requirements of this part." In discussing its decision to adopt section 154.1(d), the Commission stated in Order No. 582:

> The use of forms of service agreements as the basis of contracts between a pipeline and its customers ensures that there are no unreasonable differences among the rates, charges, services, facilities, or otherwise of the pipeline's customers....
>
> The Commission agrees that "materiality" is likely to vary with the circumstances of the case. Therefore, it is better to allow the term to remain less strictly defined in order that the particular facts of a given contract will determine whether the deviation is material and needs to be filed.... [R]ates that fall between the maximum and minimum rates permitted for the rate schedule would not be considered to be material.[11]

On rehearing of the March 28, 2001 order, the Commission again has examined the relevant tariff provision, the bid specifications, and section 9.5 of the Block I contract and finds that, while the precise wording of section 9.5 is not included in El Paso

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[10]PG&E and Edison cite El Paso Natural Gas Co., 88 FERC ¶ 61,139 at 61,407 (1999), order on reh'g, El Paso Natural Gas Co., 89 FERC ¶ 61,073 at 61,227 (1999); El Paso Natural Gas Co., 90 FERC ¶ 61,050 at 61,216 (2000).

[11]Filing and Reporting Requirements for Interstate Natural Gas Company Rate Schedules and Tariffs, Order No. 582, FERC Stats. & Regs., Regulations Preambles January 1991 - June 1996 ¶ 31,025 at 31,384-85 (1995).

Pipeline's pro forma service agreement, the addition of section 9.5 to the Block I contract does not constitute a material deviation from the pro forma agreement. It merely allows the shipper to elect to pay the maximum Commission-approved rate for higher priority rights that have been established in El Paso Pipeline's tariff. Until it exercised that option, El Paso Merchant paid a discounted rate for less valuable receipt point access.

Section 4.5(b)(i) of the GT&C of El Paso Pipeline's tariff provides as follows:

> Block I - A block of 500 MMCF/D of turned-back capacity shall be given alternate receipt point access rights to all system receipt points; provided, however, capacity sold from Block I for the maximum tariff rate set forth in Rate Schedule FT-1 shall have primary receipt point access rights to system receipt points in the Permian and Anadarko Basins.

El Paso Pipeline's bid specifications for the February 2000 open season contained the following provision applicable to Block I capacity:

> Pursuant to Section 4.5(b)(i) of the General Terms and Conditions of the Tariff, any Block I capacity awarded under this Open Posting: (i) shall have primary receipt point rights from the Mainline Anadarko ... or Mainline Permian ... receipt points only if the bidder agrees to pay the applicable maximum Tariff rates as they exist from time to time (i.e., the maximum Tariff rates at a 100% load factor); and (ii) shall have alternate receipt point rights from any mainline San Juan ... receipt point regardless of the amount the bidder agrees to pay. In the event Block I capacity is awarded under this Open Posting at a rate less than the applicable maximum Tariff rate, then such capacity shall have only alternate receipt point rights from all receipt points.[12]

Section 9.5 of the Block I contract provides as follows:

> Transportation service under this Agreement provides Shipper with alternate receipt point rights pursuant to Section 4.5(b)(i) of El Paso's Tariff. However, Shipper, or any Acquiring Shipper, may obtain primary receipt point rights from the

[12] See Ex. PUC-12 at 3.

> Anadarko or Permian Basins if Shipper under this Agreement agrees to pay El Paso the applicable 100% load factor maximum tariff rates and the Parties execute revised Exhibits A and B to reflect the primary status of the receipt points and to specify the maximum daily quantity for the related delivery points.[13]

The Commission finds no inconsistency in these provisions. As discussed above, the tariff provision provides for less valuable rights if the shipper pays less than the maximum rate, but it also allows a shipper to obtain more valuable primary receipt point rights in the Permian and Anadarko basins if it pays the maximum Commission-approved tariff rate. The same is true of the bid specifications applicable to the Block I capacity. The cited provisions of these documents do not prohibit a shipper from agreeing initially to pay a discounted rate for less valuable rights and subsequently agreeing to pay a Commission-approved higher rate for more valuable receipt point access. Further, CPUC and the intervenors have not shown that inclusion of this option in the Block I contract results in "unreasonable differences among the rates, charges, services, facilities, or otherwise of the pipeline's customers," which section 154.1(d) is intended to prevent. The Commission is satisfied that El Paso Pipeline and El Paso Merchant negotiated an option that is consistent with a tariff provision arising out of the El Paso Settlement.

The Commission's holding on this issue is consistent with previous Commission orders addressing discounting and use of alternate receipt or delivery points. For example, in El Paso Natural Gas Co.,[14] the Commission pointed out that it permits, but does not require, pipelines to offer discounts below their maximum just and reasonable rates. If the shipper receiving the discount utilizes alternate receipt or delivery points, the market and economic conditions may differ; therefore, absent express agreement that a discount will be retained for alternate points, the shipper is subject to paying the maximum just and reasonable rate for the alternate points.[15]

In addition, CPUC and the intervenors have not shown that other aspects of the transaction override these considerations and mandate Commission review under section 4. Specifically, the Commission does not find that the size of the transaction or the parties' affiliate relationship require Commission review of the contracts. In its order

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[13] See Ex. PUC-14 at 6.

[14] 62 FERC ¶ 61,311 (1993).

[15] See also Questar Pipeline Company v. PacifiCorp, 70 FERC ¶ 61,328 (1995).

addressing the Enron Contracts, the Commission stated, "Size alone has not been grounds for rejecting a transportation agreement, nor is the affiliation of a producer and a pipeline."[16] To adopt the arguments raised now on rehearing would require the Commission to limit the amount of capacity that could be held by an affiliate on the basis of the affiliation alone, effectively expanding the scope of the Affiliate Standards beyond their current application.[17] The Commission believes that such far-reaching policy considerations are addressed more appropriately in a generic proceeding, rather than on the record of this case.

The Commission's section 4 review of the Dynegy and Enron Contracts is distinguishable and does not compel a section 4 review in this case. Those contracts clearly contained material deviations from the pro forma agreements and properly were filed by El Paso Pipeline for Commission review. CPUC acknowledges as much in its request for rehearing.[18]

In particular, the complex Reservation Reduction Mechanism (RRM) in the Dynegy contracts provided for El Paso Pipeline to credit to Dynegy's monthly minimum revenue obligation a portion of IT revenues generated by volumes in excess of a threshold based on historical IT volumes, but the crediting could not exceed any shortfall Dynegy might experience in meeting its monthly minimum revenue requirement.[19] The Enron contracts also contained a revenue sharing agreement less complex than the RRM, but likewise not found in the pro forma service agreements of El Paso Pipeline's tariff.[20]

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[16] El Paso Natural Gas Co., 90 FERC ¶ 61,050 at 61,216 (2000).

[17] The Commission rejected such structural limitations in favor of implementing standards of conduct governing pipelines with marketing affiliates. See Inquiry Into Alleged Anticompetitive Practices Related to Marketing Affiliates, Order No. 497, FERC Stats. & Regs., Regulations Preambles 1986-1990 ¶ 30,820 at 31,129 (1988).

[18] Request for Rehearing of the Public Utilities Commission of the State of California, April 27, 2001, at 16. See also Pub. Util. Comm. of California v. FERC, 236 F.3d 708, 713 (D.C. Cir. 2001) ("Because [the El Paso Merchant] contract conformed to the standard contract in El Paso's tariff, El Paso was not required to obtain FERC's approval.").

[19] El Paso Natural Gas Co., 83 FERC ¶ 61,286 at 62,188-89 (1998).

[20] El Paso Natural Gas Co., 90 FERC ¶ 61,050 at 61,217 (2000).

PG&E and Edison place heavy reliance on Opinion No. 256 and subsequent Commission and Court orders in that proceeding. PG&E and Edison summarize their interpretation of those orders as follows:

> The teaching of Opinion No. 256, and the Court of Appeals' decision in TransCanada, is that the Commission has an obligation to review jurisdictional pipeline transactions, and cannot automatically apply a regulation purporting to waive Section 4 review, in circumstances where a waiver would deprive the Commission of an opportunity to conduct a meaningful review under Section 4.[21]

Although the Commission has determined that section 4 review of the El Paso Contracts is not required, it has not "automatically applied a regulation purporting to waive Section 4 review," nor has it rejected an "opportunity to conduct a meaningful review." The Commission has found no basis for requiring section 4 review of the El Paso Contracts simply because the parties are affiliates and the transaction covers a large volume of capacity. As discussed above, the Commission is setting for hearing the allegations of affiliate abuse and possible violations of the Affiliate Standards. Moreover, the market power issue, which is at the heart of this proceeding, is being examined at the hearing established by the March 28, 2001 order. The Commission is satisfied that the extensive record in the case, which will be supplemented by the record established at the hearing, provides the Commission an opportunity for a meaningful review of the El Paso Contracts and their effects, consistent with its statutory obligations under the NGA. Therefore, the Commission denies the requests for rehearing on this issue.

C. Block II Recall Rights

PG&E and Edison state that the Commission did not address its request that El Paso Pipeline be required to comply with the El Paso Settlement with respect to the Block II recall rights or to refund the $58.4 million PG&E paid for these rights, plus interest. Specifically, PG&E and Edison claim that CPUC documented that, in July 2000, El Paso Pipeline refused to allow PG&E's Core Procurement Department to recall discounted

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[21] Joint Request of Pacific Gas and Electric Company and Southern California Edison Company for Rehearing and Clarification, April 27, 2001, at 11.

Block II capacity from El Paso Merchant at less than maximum rate in accordance with the El Paso Settlement and section 4.1 of El Paso Pipeline's tariff.[22]

In an answer filed October 16, 2000,[23] the CPUC pointed out that the recall rights for Block II capacity provide the only discounted access to the San Juan Basin for certain shippers serving northern California. However, CPUC asserted that El Paso Pipeline responded to the recalls by advising El Paso Merchant how to re-recall the capacity and by unilaterally deciding that its recall tariff provision, which merely requires a matching of El Paso Merchant's $.065/MMBtu rate, no longer applied. Instead, stated CPUC, El Paso Pipeline decided that maximum transportation rates were necessary for a recall.[24]

CPUC disputed El Paso Pipeline's contention that El Paso Merchant's use of Block II capacity was not subject to recall in July or August 2000 because El Paso Merchant's limited use of Block II capacity at that time was to transport natural gas to northern California. However, CPUC asserted that El Paso Merchant did not use most of its Block II capacity rights during the summer of 2000.[25]

Further, contended CPUC, El Paso Merchant used Block II capacity at the Mojave delivery point in March, April, and June 2000 and at the SoCalGas delivery point at

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[22] PG&E and Edison cite Ex. PUC-1 at 35-37, Ex. PUC-35. PG&E and Edison also cite the following from the Commission's discussion of the Block II recall rights in conjunction with the Dynegy contracts:

> El Paso shall recall the capacity if Block II Shipper(s) requesting the capacity at least match the rate in the contract covering the capacity to be recalled and subscribe such capacity for more than one month. This language, and the related language dealing with recalls of capacity for a period of one month or less, is clearly obligatory in nature.

El Paso Natural Gas Co., 88 FERC ¶ 61,139 at 61,421 (1999).

[23] Motion for Leave to File Answer and Answer of the Public Utilities Commission of the State of California to Respondents' Answers to Motion for Summary Disposition, October 16, 2000, at 26-28.

[24] CPUC cites Ex. PUC-1 at 35-37; Ex. PUC-34; Ex. PUC-35.

[25] CPUC cites Ex. PUC-1 at 32; Ex. PUC-31.

Ehrenberg in June 2000.[26] According to CPUC, neither of these delivery points serves northern California. Further, argued CPUC, even if El Paso Merchant stopped using these other delivery points in July and thereafter, it should not be able to stop recalls of this Block II capacity.

El Paso Pipeline disputed CPUC's position. El Paso Pipeline acknowledged that Block II capacity could be recalled by a northern California shipper at El Paso Merchant's contract rate, but only when certain conditions were met: (1) the Block II capacity is being used for service to another market area, and (2) the Block II shipper first acquires any unmarketed Block II capacity. El Paso Pipeline asserted that the recall requests cited by CPUC failed to satisfy the first of these conditions. According to El Paso Pipeline, when PG&E requested a recall of Block II capacity, none of El Paso Merchant's Block II capacity was being used for deliveries to a non-northern California market and thus was not subject to recall.

Although the PG&E letter cited by the CPUC refers to other purchases of discounted Block II capacity, El Paso Pipeline maintained that, when these purchases occurred, the discounted El Paso Merchant Block II capacity was being used for deliveries outside northern California and was subject to recall.

The Commission finds no merit to the argument raised by CPUC, PG&E, and Edison with respect to the recall of Block II capacity. El Paso Pipeline's tariff and previous Commission orders have made it clear that shippers serving PG&E's service territory through the PG&E-Topock delivery point have limited reserved rights to the Block II capacity. Specifically, when Block II capacity is not being utilized to serve PG&E's service territory, it may be recalled to serve that territory under certain prescribed circumstances.[27]

Adopting the position urged by CPUC, PG&E, and Edison would mean that, simply because Block II capacity utilized non-Topock delivery points at one time, the capacity should thereafter be subject to recall at less than the maximum rate. The Commission disagrees. At times when the Block II capacity is utilizing alternate delivery points, Block II shippers may recall it to serve PG&E's service territory. Depending on the duration of the requested recall, the recalling party may be required to match only the contract rate for the capacity or may be required to pay the maximum rate. However, when PG&E's affiliate requested the recall in July 2000, the evidence shows that El Paso

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[26] CPUC cites Ex. PUC-26.

[27] See El Paso Natural Gas Co., 83 FERC ¶ 61,286 at 62,200 (1998).

Merchant's Block II capacity was utilizing the PG&E-Topock delivery point.[28] The successful Block II recall requests cited by PG&E were made in June 2000, when other delivery points in addition to Topock were being utilized,[29] and the capacity utilizing those alternate delivery points was subject to recall by matching the contract price because the terms exceeded one month.[30] Accordingly, the Commission denies rehearing on this issue.

D. Hearing on the Market Power Issue

On rehearing, El Paso Pipeline and El Paso Merchant ask the Commission to reverse its decision to establish a hearing on the market power issue and to dismiss this case. They maintain that the complaining parties, who bear the burden of proof under NGA section 5, failed to establish a prima facie case justifying the hearing. They point out that the Commission recognized that the CPUC failed to provide any market power study in support of its claim and that The Brattle Group study submitted by Edison admits that it does not address the numerous factors affecting California gas prices. El Paso Pipeline argues that a hearing is unnecessary because the Commission found the El Paso Contracts to be lawful and consistent with Commission precedent.

El Paso Merchant points to CPUC's responses to data requests in support of its claim that CPUC failed to carry its burden of proof. El Paso Merchant contends that the data responses show that CPUC failed to establish El Paso Merchant's alleged market power, to consider other relevant factors affecting gas prices in California, and otherwise to substantiate its allegations. Additionally, El Paso Merchant states that the complaining parties and the Commission failed to consider evidence that El Paso Merchant had an incentive to flow as much capacity as possible in order to offset financial losses from its hedging activities. Finally, El Paso Merchant argues that dismissal of the complaint would be consistent with recent relevant Commission findings on the energy situation in California.

The Commission denies rehearing on this issue. In this proceeding, the Commission determined that the evidence available at the time of the March 28, 2001 order did not provide an adequate basis for resolving the dispute concerning the market

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[28] See Ex. PUC-35; Ex. PUC-26.

[29] See Ex. PUC-33.

[30] El Paso Natural Gas Company, FERC Gas Tariff, Second Revised Volume No. 1-A, Section 4.5(b)(ii).

power allegation.[31] It now is setting the affiliate abuse issues for hearing. Absent evidence of an abuse of discretion, which El Paso Pipeline and El Paso Merchant have not shown on rehearing, the Commission's decision to hold a trial-type hearing is conclusive.

E. Remedies

PG&E and Edison ask the Commission to clarify what potential remedies are available if the ALJ determines that El Paso Pipeline and El Paso Merchant exercised market power. At a minimum, PG&E and Edison ask the Commission to clarify that the ALJ may require El Paso Merchant to disgorge all past profits obtained during periods when they claim El Paso Pipeline and El Paso Merchant exercised market power.[32]

The Commission will defer consideration of PG&E's and Edison's request for clarification concerning potential remedies. The Commission views it as premature to address the subject of remedies unless the hearing demonstrates violations by El Paso Pipeline and El Paso Merchant with respect to the issues set for hearing.

F. Conclusion

As discussed above, the Commission is setting for hearing the issues relating to the allegations of affiliate abuse and possible violations of the Affiliate Standards raised by the complaint in this proceeding. The Commission grants the Chief Judge the discretion to restructure the hearing proceedings to accept additional testimony regarding these allegations. The Commission also suspends the June 4, 2001 Notice of Extension of Time, which extended until September 4, 2001, the deadline for the Chief Judge's initial decision. The Chief Judge shall report to the Commission within 10 days of the date of

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[31] In a recent revision of its complaint procedures, the Commission recognized that some complaints can be decided on the basis of the pleadings alone if they involve discrete issues not requiring development of a record before an ALJ. However, when complaints are not appropriate for consideration on the pleadings alone, the Commission will set them for a trial-type hearing. Complaint Procedures, Order No. 602, FERC Stats. & Regs., Regulations Preambles July 1996 - December 2000 ¶ 31,071 at 30,765 (1999).

[32] PG&E and Edison cite Public Utilities Commission of the State of California v. FERC, 143 F.3d 610 (D.C. Cir. 1998) (directing FERC to determine appropriate remedy where a FERC jurisdictional rate was illegally charged and intrastate pipeline collected a "windfall profit"); Washington Water Power Co., 83 FERC ¶ 61,282 (1998).

issuance of this order a revised hearing schedule and his recommended schedule for expedited issuance of an initial decision on all matters set for hearing.

The Commission orders:

(A) Rehearing of the March 28, 2001 order is granted and denied, as discussed in the body of this order.

(B) Within 10 days of the date of issuance of this order, the Chief Judge shall report to the Commission a revised hearing schedule and his recommended schedule for expedited issuance of an initial decision, as discussed in the body of this order.

By the Commission. Chairman Hébert and Commissioner Wood concurred with separate statements attached.

(S E A L)

David P. Boergers,
Secretary.

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Public Utilities Commission of the
State of California

Docket Nos. RP00-241-000
and RP00-241-004

v.

El Paso Natural Gas Company,
El Paso Merchant Energy-Gas, L.P.,
and El Paso Merchant Energy Company

(Issued June 11, 2001)

Chairman Hébert, *concurring*:

In this order the Commission expands the scope of the hearing in this proceeding to include the issue of whether El Paso Pipeline or El Paso Merchant engaged in affiliate abuse or violated the Commission's affiliate standards in bidding for or awarding the El Paso contracts, including the transportation discount granted by Mojave. My interest in ascertaining all the facts pertaining to the anomalous natural gas price situation for the state of California versus the rest of the nation has always been great and I believe that the Commission is responding appropriately to the Chief Administrative Law Judge's request for guidance and to the various requests for rehearing submitted regarding this issue. Accordingly, I believe that the Commission's review of this matter will be advanced by a more extensive factual record derived with all the obligations and protections of a full evidentiary hearing for all parties.

I recognize the seriousness of natural gas prices in the California market and I am committed to providing all Commission resources to determine the actuality of that price situation. I believe that all the parties involved, and most importantly the American consumer, have the right to know, as soon as possible, the outcome of this proceeding. Within two months of my Chairmanship this proceeding was before the entire Commission for disposition. Rehearing has been provided in a timely manner. I remain committed to ensuring that certainty from this forum will be provided to all in an expeditious manner.

Chairman Curt L. Hébert, Jr.

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WOOD, Commissioner, concurring:

I support the Commission's order and write separately only to state a general policy preference that the procedural history of this case raised in my mind. This complaint was filed in April 2000. In the framework of active energy markets, it is critical that the Commission act expeditiously on complaints. Where underlying disputed facts must be determined before concluding that a complaint has merit, it best serves competitive markets to refer those issues immediately to a trier of fact. As appropriate, the Commission can, and should, frame such cases up front with our determinations on matters of legal and policy interpretation, but disputed fact issues are best reviewed before an Administrative Law Judge.

In overseeing competitive energy markets as a joint effort with our colleagues at state commissions, it is critical that the FERC be seen as a watchful and vigilant partner. Expeditious referral and action on filed complaints is a central tool in our market oversight toolbox.

Respectfully submitted,

Pat Wood, III
Commissioner